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SECRET AND PERSONAL

COPY NO 1 OF 2

PRIME MINISTER

De la M...

PUBLIC EXPENDITURE

I told you this morning that after immense struggles, considerable hostility and a great deal of pressure, and to the surprise of my key advisers, I managed to obtain from the gas and electricity industries improvements on their bids of £1,600 million pre-tax.

My advisers, who include a number of very experienced practitioners in the game of public expenditure cuts, were very surprised that I went to the Star Chamber and said that I might, as a last ditch exercise, using every power and persuasion at my command, get a further £300 million pre-tax from the industries bringing the total figure to £1,900 million.

I well understand your requiring still more if it can be obtained. I do assure you, however, that there is no way you will obtain more without a colossal battle with both the gas and electricity industries - with all of their boards and consumer organisations mobilised against us. If we legislated to achieve what we required the legislation would be impossible. I can assure you I really have used considerable negotiating skills to push them thus far without making them decide to go in for a fight.

This morning you expressed to me your particular difficulty in the third year. I have urgently examined my proposals in depth and could rearrange events so as to improve the third year, switching £147 million from the previous years and taking a complete risk in undertaking to find an additional £20 million above what had been previously promised. This therefore means I am back to baseline in the first two years in spite of the enormous impact of

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Corporation Tax which accounted for virtually the whole of the excess above baseline. In the third year I am within £48 million of the baseline, in spite of the fact that in that year the Chancellor will benefit from £1.3 billion Corporation Tax.

As I told you this morning, in 1979 when we came to power the gas and electricity industries contributed a total of £283 million. Over the three years covered by these IFR proposals, if I achieve the target I am endeavouring to achieve, the Government will receive nearly £9 billion from these two industries. As you know I personally strongly question the justification for this. I have recognised however that it is the collective view of you and your Government, and I really have done much more to achieve that collective view than any of those surrounding me considered was possible.

I mentioned to you at the end of our meeting that, if for presentational reasons, you wish to do anything for any one of the years, including the third year, it would be possible to change the basis for the payment of the gas levy. This would have no economic effect but would improve the public expenditure figures by some £330 million in the year of the change without any effect on the PSBR. Were you to decide to do it in the third year it would of course be odd to take credit for doing it three years in advance. I in no way advocate this change but I mention it as a possible recourse at a time of difficulty.

If the Government decides to accept these proposals I would naturally do my best to speedily obtain the £1,920 million pre-tax I am hoping to obtain. I must state very clearly however that I not only think it impossible to obtain more, but, should such an attempt be made, quite a lot of the £1,920 million may disappear.



Secretary of State for Energy

5 November 1984

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GT. S. DART.

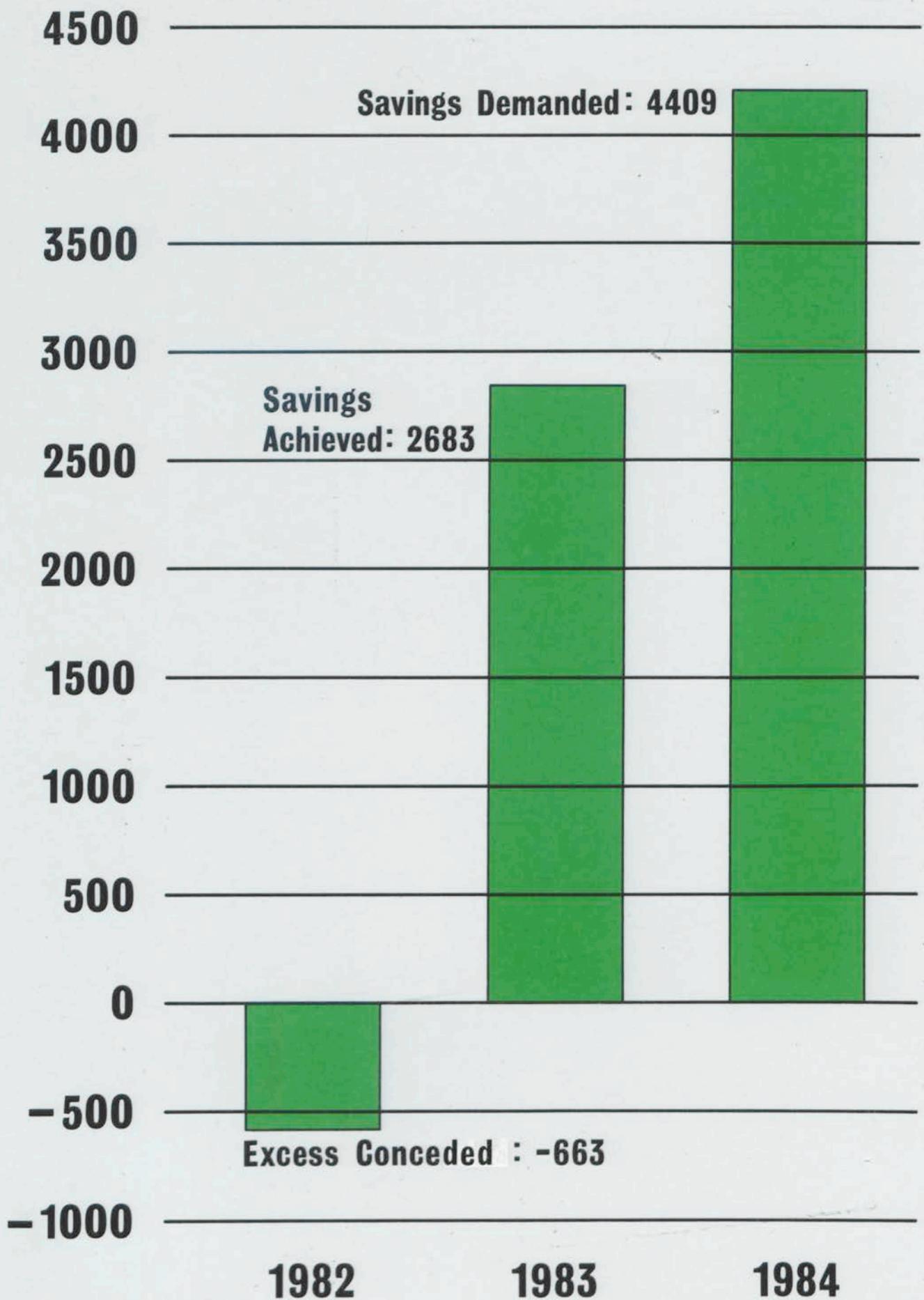
IFR 1984

DEPARTMENT OF ENERGY

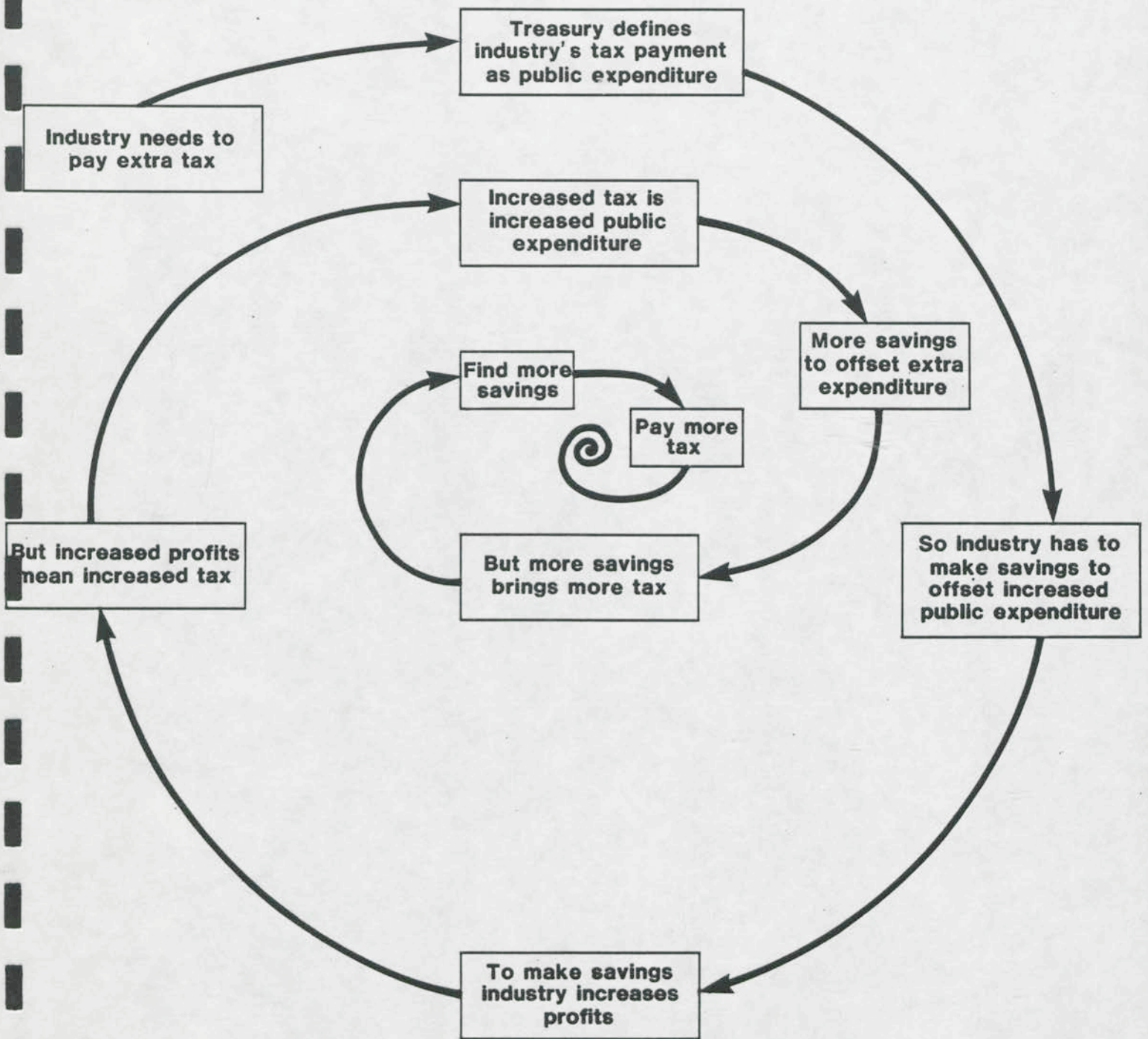
19 OCTOBER 1984

IFR - ENERGY INDUSTRIES

£m (Outcome compared with industry bids)

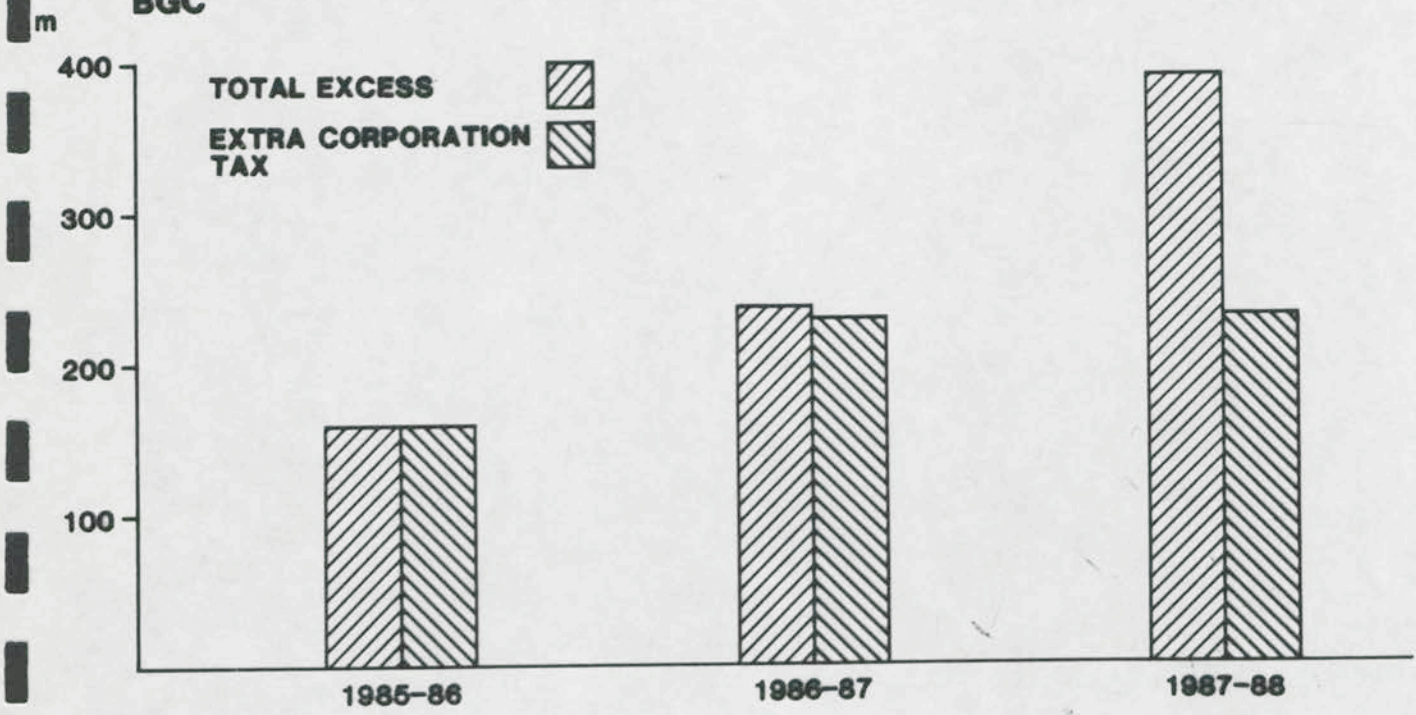


THE VICIOUS SPIRAL

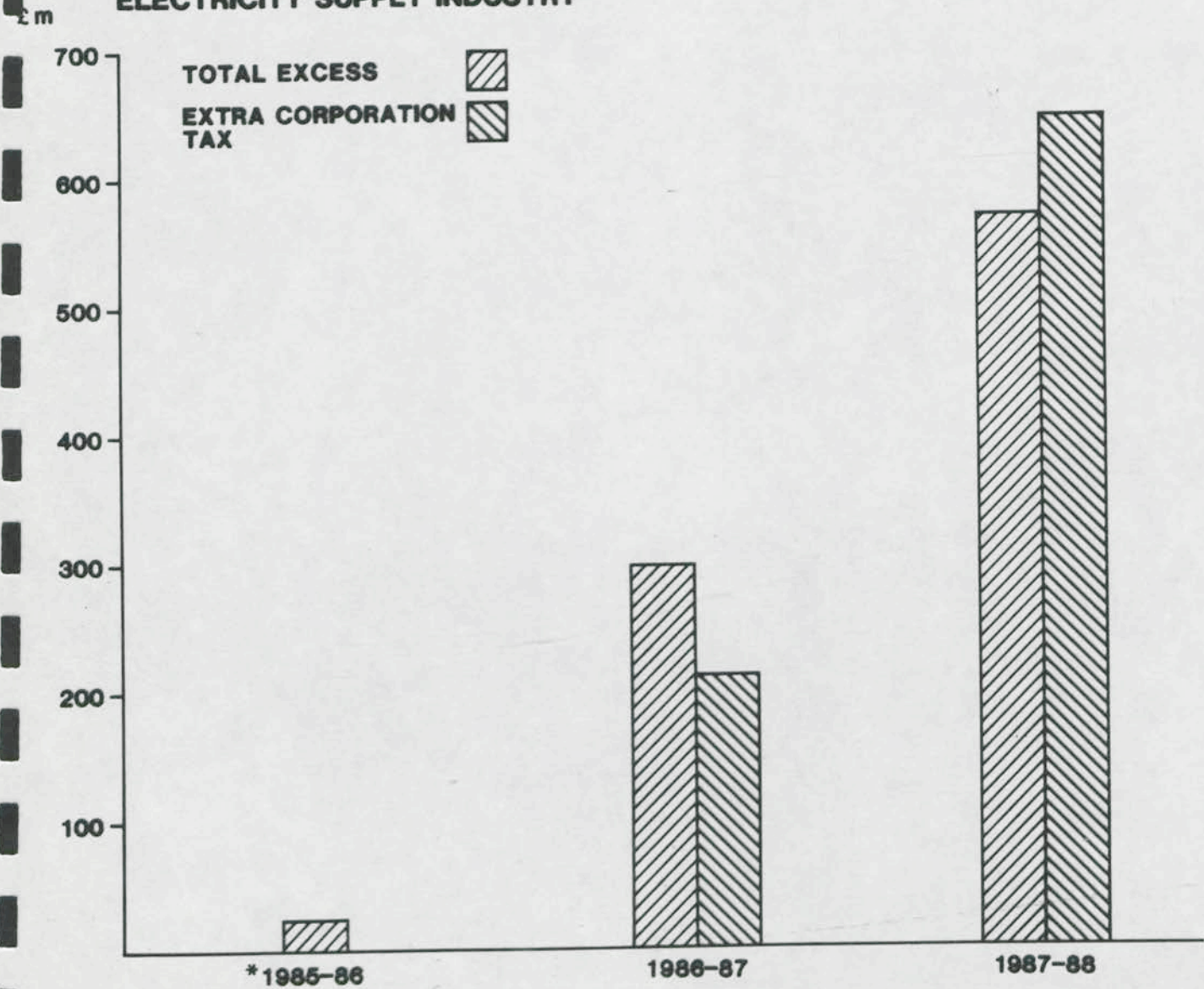


IFR 1984: ALMOST ALL THE EXCESS (88%) ABOVE BASELINE IS DUE TO EXTRA CORPORATION TAX

BGC



ELECTRICITY SUPPLY INDUSTRY

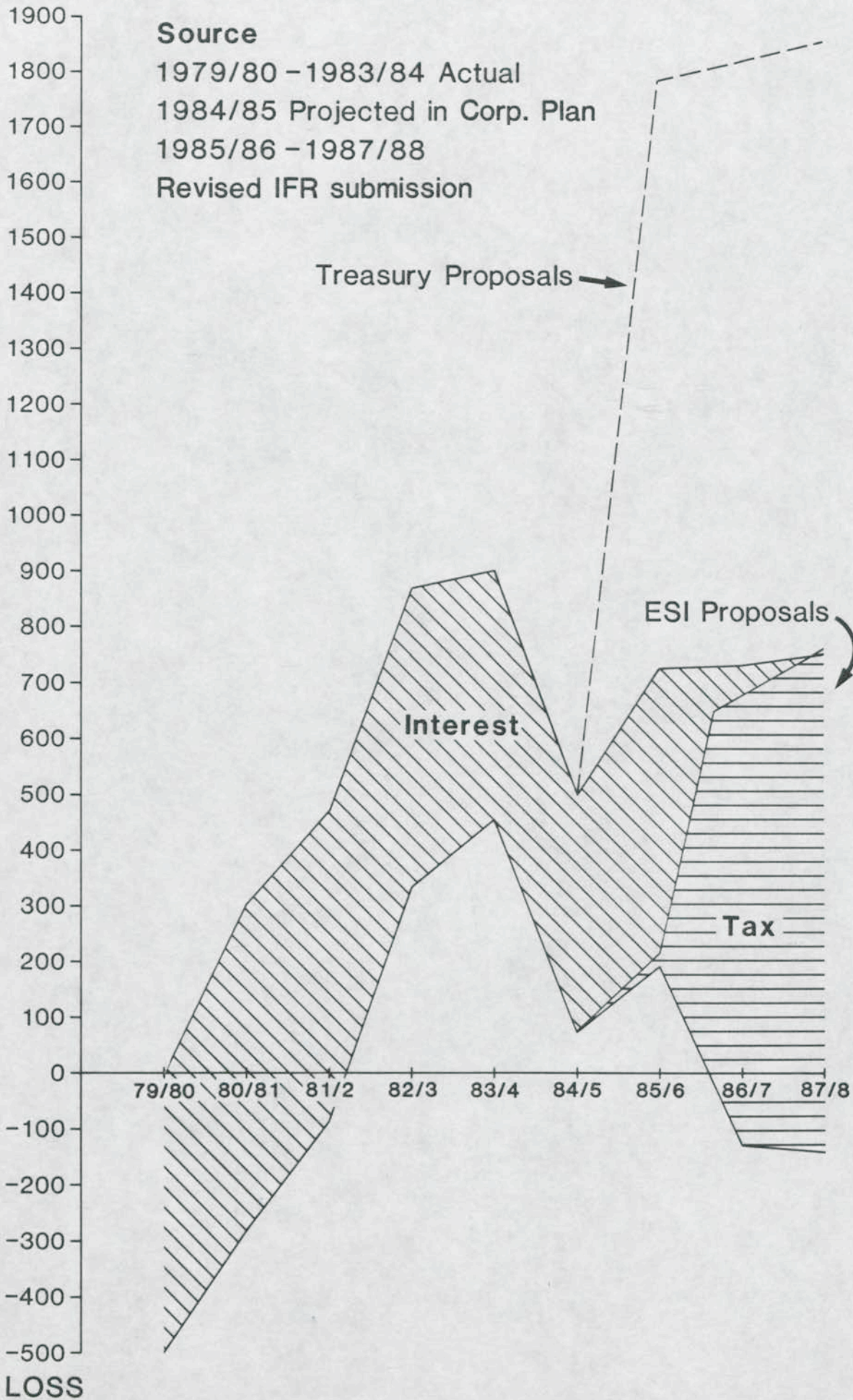


* No Corporation Tax payable in 1985-86

ESI Operating & Post-Tax Profit

CHART D

£m PROFIT



BGC Operating & Post-Tax Profit

CHART E

Source

1979/80 - 1983/84 Actual

1984/85 onwards : Corporate Plan/IFR

